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Nos. 20378, 20447 and 20522

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

FEDERAL HOME LOAN BANK BOARD, ET AL.,

Appellants

v.

SIDNEY ELLIOTT, ET AL.,

Appellees

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

BRIEF FOR APPELLANTS FEDERAL HOME LOAN BANK BOARD AND FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

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JURISDICTIONAL STATEMENT

These are appeals[1/] by the appellants Federal Home Loan Ban Board ("Board") and Federal Savings and Loan Insurance Corporatc ("Insurance Corporation") from three judgments, all substantialy similar, entered by the United States District Court for the Southern District of California (Peirson M. Hall, J.) on May 17 1965 (1R 697-761; 2R 907-971; 3R 1642-1706). The judgments wer entered following the granting by the District Court of motions for summary judgments filed by the appellees in three actions instituted to have declared invalid those terms of a Merger Agr ment, dated June 12, 1963, between Long Beach Federal Savings a Loan Association ("Long Beach") and Equitable Savings and Loan Association ("Equitable") which obligated Equitable to distribu 791,650 shares of its guarantee stock to Long Beach shareholder in accordance with the formula set forth in the Merger Agreemen (Exh. E, pp. 44-50). The appellees, in substance, prayed for a judicial determination that the Equitable guarantee stock shoul be distributed on a pro rata basis rather than in the manner pr vided by the Merger Agreement, even though the Merger Agreement

1/ By stipulation of the parties and orders of this Court, dat November 6, 1965, the appeals have been consolidated for motion briefing and argument. References in this brief and its Append to the original papers in No. 20378 (D.C. No. 63-1072 PH), No. 20447 (D.C. No. 63-1230 PH) and No. 20522 (D.C. No. 63-1107 PH) are designated "1R", "2R" and "3R", respectively. References t the transcript of the proceedings in the District Court are designated "Tr.".

or to the consummation of the merger on September 10, 1963, been approved by the Board and by the California Savings and n Commissioner ("California Commissioner"), also an appellant, er and in accordance with, respectively, federal and state law, well as by the shareholders of Long Beach and the stockholders Equitable. (Exhs. D1-D9.)

The first District Court action (No. 63-1072 PH) was in-tuted on September 10, 1963 by Long Beach and four individuals stituting the Shareholders' Protective Committee of Long Beach eral Savings and Loan Association ("Shareholders' Protective mittee"), the latter suing as individuals, as the Shareholders' tective Committee, and as representatives of the entire class Long Beach savings shareholders.[2/] The defendants in this ion, described as one to quiet title and for declaratory relief, e the Board and the Insurance Corporation. Jurisdiction of the trict Court was invoked under 28 U.S.C. 1331 and 1391(e) and J.S.C. 1464(a), 1464(b), 1464(c), 1464(d) and 1725 (1R 3, 4).

The District Court held that the Shareholders' Protective nittee represented, with certain exceptions not relevant here, Long Beach shareholders, including those who were adversely ected by the position taken by that committee in the litigation by the District Court's judgments (1R 312-315A; 2R 407-412; 512-317). The Shareholders' Protective Committee could not sibly represent shareholders who were so affected by the liti-on and the judgments. Sam Fox Publishing Co. v. United States, U.S. 683 (1961); Hansberry v. Lee, 311 U.S. 32 (1940); Horton Citizens Nat. Trust & Savings Bank of Los Angeles, 86 C.A. 2d , 195 P. 2d 494 (1948). The Board has the right to and does resent the interests in this litigation of such Long Beach share-lers. Reich v. Webb, 336 F. 2d 153 (9th Cir., 1964), cert. den. U.S. 915 (1965). See also Borak v. J. I. Case & Company, 317 d 838, 845 (7th Cir., 1963), aff'd. 377 U.S. 426.

On the same day the foregoing action was commenced, September 10, 1963, a similar action was filed in the Californi Superior Court (No. SOC 6367) by the Shareholders' Protective C mittee suing in the same capacity as in the District Court acti Named as defendants were Long Beach, Equitable, John Does 1-70, the Board and the Insurance Corporation. This action was also described as one to quiet title and for declaratory relief (2R Long Beach and Equitable on October 8, 1963 attached their resp complaints in District Court action No. 63-1072 PH and District Court action No. 63-1107 PH declaring said complaints to be the respective answers, counterclaims and cross-claims in this stat court action (2R 37-45). The Board and the Insurance Corporati on October 10, 1963 removed this action to the District Court (Action No. 63-1230 PH) under 28 U.S.C. 1441 and 1442(a)(1) (2R

The third action was filed on September 17, 1963 in the District Court (No. 63-1107 PH) by Equitable against the Share- holders' Protective Committee, the Board, the Insurance Corpora Long Beach and some individual Long Beach shareholders. This a was described as one in interpleader and for declaratory relief Equitable depositing with the Clerk of the Court the 791,650 sh of its guarantee stock which it was contractually obligated to tribute to Long Beach shareholders in accordance with the terms the Merger Agreement. Jurisdiction of the District Court was i under 12 U.S.C. 1464, 1464(d), 1725, 28 U.S.C. 1331, 1335, 1397 F.R.C.P. Rule 22, and the District Court's general equity inter

vers (3R 1-17B). In this action Long Beach filed its complaint Civil Action No. 63-1072 PH as its answer, counterclaim and oss-claim (3R 64-66). Similarly the Shareholders' Protective mmittee filed its complaint in the removed state court action o. 63-1230 PH) as its answer, counterclaim and cross-claim in is third action (3R 64-66).

During the course of the proceedings below the appellant ifornia Commissioner was added as a party defendant in Civil ions No. 63-1107 PH and No. 63-1230 PH (2R 601-612; 3R 425a-c) and Equitable was added as a party defendant in Civil ion No. 63-1072 PH (1R 589-590).[3/] The California Commissioner ved to dismiss the two actions in which he had been added as a ty, challenging the District Court's jurisdiction on the und of sovereign immunity (2R 675-678; 3R 606-607). The Board the Insurance Corporation contended that the California missioner was an indispensable party in all three actions and t if he was not subject to the jurisdiction of the District rt, the actions had to be dismissed (1R 369; 2R 465; 3R 358). District Court denied the two motions to dismiss filed by the ifornia Commissioner (2R 728-729; 3R 653-654).

Appellee N. Joseph Ross, a former large account holder at Long ch, also intervened as a party in the three actions, taking the e position in the litigation as that of the other appellees.

The District Court, in its memorandum opinion granting appellees' motions for summary judgment and requiring distributi of the guarantee stock on a pro rata basis ruled that the Califr Commissioner was subject to its jurisdiction and that it had jui diction of the parties and the subject matter of the actions un the Interpleader and Declaratory Relief Statutes, the Home Owne Loan Act of 1933, as amended, and the Administrative Procedure 28 U.S.C. 1335, 1397, 2201, 2202, 2361; F.R.C.P. 12, 22, 56(a), 57; 12 U.S.C. 1464(d)(1), 1725(c)(4); and 5 U.S.C. 1009 (1R 554 590; 3R 1477-1512).

This Court has jurisdiction of the appeals under 28 U.S.C. 1291.

STATEMENT OF THE CASE

1. The Facts

Commencing in 1946, Long Beach and the Board became involv in a series of controversies arising out of the action of the Board in taking over the management of Long Beach on two occasi in 1946 and 1960, pursuant to the authority granted it in the Home Owners' Loan Act of 1933, as amended (12 U.S.C. 1461 et se The take-overs resulted from the Board's determinations that Lo Beach had engaged in certain unsound financial operations. Whe the Board was correct or not was never adjudicated despite the rash of litigation which ensued (Exh. E, p. 16; Exh. 8, pp. 1-3)

4/ The reported decisions rendered in the course of this exten litigation are compiled in the District Court's opinion. Elliot et al. v. Federal Home Loan Bank Board, 233 F. Supp. 578, 584 (S Calif., 1964), n. 1. Except as background material the facts ar issues of those controversies are not involved in the present li gation.

On February 14, 1962, a settlement agreement ("Settlement eement") was entered into by and among Long Beach, the Board the Insurance Corporation,[5/] which provided, inter alia, for the missal of all then pending litigation between the Board, the urance Corporation and Long Beach and the return of Long Beach its private management. In addition, Long Beach was given the ht, if it so chose, to liquidate pursuant to a specific plan forth in Article XV of the Settlement Agreement, about which e will be said later, infra, pp. 34-37, (Exh. 8, pp. 43-48).

During the settlement negotiations, representatives of the rd expressed their concern that after the return of Long Beach its private management "publicity about Long Beach's proposed uidation might result in the influx into the Association of ounts, invested, not for the purpose of carrying out the pro-ions of the Home Owners' Loan Act of 1933, as amended, but to ble the depositors to participate in the distribution of Long ch's net worth, which would dilute the interests of the bona e Long Beach shareholders." (Wilfand affdvt., 3R 1373). Long ch was a mutual association owned by its savings account holders her than by the stockholders as in a stock association such as itable. The book net worth of Long Beach as of the year ending ember 31, 1961 exceeded $7 million (Exh. E, p. 22).

While the Insurance Corporation, the operations of which are ected by the Board, is also an appellant, it has no real part play in the present controversy.

A basis for concern was "increased savings account activity during the period of negotiations (McMurray affdvt., 3R 999). T Board's then General Counsel suggested that only persons who hac been Long Beach members on April 22, 1960, the date the Board la took over management of Long Beach and when savings accounts amounted to $95 million, be permitted to again become members to share in the contemplated liquidation, and distribution of the r worth (Wilfand affdvt., 3R 1373). Mr. Thomas A. Gregory, the President of Long Beach, objected because he said that many pers in the Long Beach community had contributed to the growth of the Association, though they may not have been members on April 22, 1960. He stated they should also be permitted to become members (Wilfand affdvt., 3R 1373). The suggested restriction was not i corporated in the Settlement Agreement upon Long Beach's assuran that "Long Beach had never solicited accounts outside the Long Beach area and had never sought large accounts; that all new accounts would be screened to see to it that only local persons became members; and that unduly large accounts would not be accepted." (Wilfand affdvt., 3R 1373). Mr. Gregory, Long Beach President, denied having given any such assurance to the Board (Gregory affdvt., 3R 1146).

Pursuant to the Settlement Agreement Long Beach was return to its private management on April 2, 1962 (Exh. E, p. 16; McMurray affdvt., 3R 1000). At that time savings (share) accou in Long Beach totalled about $30,500,000 (McMurray affdvt., 3R

the day of the return, April 2, approximately $24 million was psited in Long Beach (McMurray affdvt., 3R 1000). As of il 30, 1962, Long Beach savings accounts had climbed to about ,800,000 (Exh. 6 to McMurray affdvt., 3R 1021). From then il November 30, 1962 the net increase in savings accounts was roximately $5,700,000, the total of all accounts amounting to ut $71,500,000 on November 30, 1962 (Exhs. 7-13 to McMurray dvt., 3R 1027-1074).

In the meantime, the Long Beach management in May 1962 had ormally submitted to the Board a proposed plan of merger between g Beach and Equitable (Exhs. C-1, C-2, C-3). In early July 1962, le negotiations were proceeding in connection with the merger posal, Mr. Gregory, the President of Long Beach and the principal otiator for Long Beach and perhaps for Equitable,[6/] advised the rd about large withdrawals which had been made from Long Beach, r the payment of the June 30, 1962 dividend, by one Mr. Louis r and some of his associates (McMurray affdvt., 3R 1000; land affdvt., 3R 1376).[7/] At the Board's request, Mr. Gregory

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Mr. Gregory was the beneficial owner of a substantial block of itable stock during the entire period of the merger negotiations . E, p. 10). In addition, his name was carried on Equitable's ionery as vice-president as late as June 20, 1963 (Exh. C-58). Gregory's sister, Mrs. Carolyn Stanaland, was the owner of a much er block of Equitable stock (Exh. E, pp. 10, 15).

Mr. Boyar and many of these associates were also investors in itable stock. (Exhs. C-15, E-15, 3R 1191, 1215.)

submitted a list of accounts of $100,000 or over which had been opened at Long Beach on and after April 2, 1962 (McMurray affdvt 3R 1000; Wilfand affdvt., 3R 1376; Exhs. C-5, C-6, C-15). That list showed that 77 such accounts, totalling in the aggregate ab $20,500,000, had been opened by, according to Mr. Gregory's char terization, "celebrities of the financial and entertainment worl widely known for their great wealth and business acumen" (Gregor affdvt., 3R 1139).[8/] This situation was in marked contrast to the situation on April 22, 1960, when Long Beach, with an aggregate total of savings accounts of approximately $96 million, had only one account in excess of $100,000 (McMurray affdvt., 3R 1001). later analysis of Long Beach accounts which increased by $10,00 or more between April 2, and November 30, 1962, made from data supplied by Long Beach (Exhs. C-29, C-29A), revealed equally marked contrasts in old and new account holdings in the $20,000 $100,000 range. In April 1960 when Long Beach had on deposit m than $96 million there was only one account in the $75,000 - $100,000 range. In the period April 2, 1962 - November 30, 196 there were six such accounts, none of the owners of which had previously been Long Beach shareholders. In April 1960 there w no accounts in the range of $50,000 to $75,000. In the period April 22, 1962 - November 30, 1962 there were 34 such accounts.

8/ Approximately $10 million of such accounts were withdrawn a the June 30, 1962 dividend (Exh. C-5, C-6, C-15).

the shareholders owning these deposits only two had previously n shareholders of Long Beach. Their balances as of April 2, 2 are not known to the appellants. In April 1960 there were accounts on deposit in the range of $20,000 to $50,000. In period April 2, 1962 - November 30, 1962 there were 124 such ounts and of these account holders 18 had previously been reholders in Long Beach. Again, their account balances as April 2, 1962 are not known to the appellants (Exhs. 18 and to McMurray affdvt., 3R 1095-1098, Exh. R).

This influx of large accounts into Long Beach, most of which e opened by persons having no prior connection with Long Beach, of grave concern to the Board (McMurray affdvt., 3R 1001-1002; , R). Equally of concern was the fact that of the aggregate al of more than $28 million in accounts which had increased by ,000 or more between April 2, 1962 and November 30, 1962, over million of such accounts were pledged as of November 30, 1962, secure loans, the principal pledgee being the City National (formerly the City National Bank of Beverly Hills) which as November 30, 1962, had outstanding loans of over $8 million, the ceeds of which loans had been deposited in Long Beach (McMurray dvt., 3R 1001; Exh. R).[9/] The inference is plain that the new reholders were motivated by some consideration other than the al return earned on savings accounts and the existence of eral savings and loan account insurance.

Mr. Hart, the President of the City National Bank, was a sub- tial stockholder in Equitable as was one of its officers, Curtis ner (Exh. E, p. 10; Exh. C-29).

The effect of this tremendous influx into Long Beach of new money in large sums, much of it borrowed for the purpose, was to dilute the interests of the small and regular shareholders in the Long Beach net worth in the event the liquidation plan of Article XV of the Settlement Agreement were followed. A similar consequence would, of course, ensue if there should be a merger and stock distribution rather than a liquidation.10/ It should also be pointed out, because of this sudden and large inflow, Long Beach was in no position to invest the new money quickly, yet had to pay a high dividend rate to the new savers (the rate ranged from 4.5% to 4.8%). As a consequence Long Beach operated at a loss of over $100,000 per month during the period January 1, 1963 to September 10, 1963 and this in turn reduced its net worth (Wilfa[illegible] affdvt., 3R 1378, 1379).

10/ The extent of the dilution, had the Board approved a pro rata distribution of Equitable stock in connection with the merger, is set forth in Long Beach's proxy statement (Exh. E, pp. 4, 5). Under the Merger Agreement formula (*infra*, p. 14), the proxy statement reads, ". . . there is about $53,000,000 in Long Beach share accounts eligible to participate in the distribution of the 791,650 shares of Equitable stock, so that one share of Equitable stock would be distributed for approximately each $67 of a member's eligible account balance. . ."

". . . The total amount of share account balances . . . excluded on November 30, 1962 was approximately $19,000,000, or about 26% of total share account balances on that date. Without such exclusion, one share of Equitable stock would be distributable for approximately each $91 of a member's account balance in Long Beach as of November 30, 1962."

Faced with what it regarded as a breach of fiduciary duty[11] the Long Beach management in permitting such a tremendous in-x of new money of this sort,[12] the Board took the position during merger negotiations that it would not approve a pro rata dis-bution of Equitable stock to Long Beach shareholders (C-42, 3). To do so would have permitted the speculating depositors, luding those who even Mr. Gregory himself characterized as pably temporary investors,[13] to share in Long Beach's net worth which they had contributed nothing.[14] Long Beach and Equitable

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The statement in the District Court's opinion that no claim made of "crime, fraud, illegality, or other wrongdoing" inst either Long Beach, Equitable or the officers or directors either (233 F. Supp. at p. 583) is incorrect. The Board's wer specifically set up the breach of fiduciary duty by the g Beach management (1R 373-374; 2R 468-469; 3R 369-370), a ition which was also taken in the Board's memoranda below 981, 1355). See also the affidavit of the then Board chairman support of the Board's motion for summary judgment (3R 1002).

The District Court's statement that the Long Beach management no power to prevent such an influx (233 F. Supp. at p. 594) is ently in error. The Long Beach by-laws (Exh. 19, §§ 6(e), 6(f)) licitly grant management such power.

Mr. Gregory's letter of July 25, 1962 (Exh. C-6) reads, "The estors opening accounts of $100,000 or more after 4/2/62, who e not withdrawn up to July 8, 1962, total $10,000,000. We are ised that approximately $7,000,000 of these accounts have been dged to banks, which might indicate the accounts are of a porary nature."

The District Court refused to allow the Board during discovery ceedings to inquire into the status of the accounts of these ge investors after September 10, 1963 (Tr. 368-371, 377-380, -395; 3R 598-600, 698-709). The Board wished to show that most, not all, of those investors had closed their accounts promptly shortly after their rights to share in the Equitable stock dis-bution had become fixed. This was the date the merger was summated, September 10, 1963.

finally agreed to insert in the merger agreement the distributi[on] provisions which were struck down by the District Court (Exhs. C-51, 52). These provisions read (Exh. E, pp. 47-48):

> "Long Beach has required waivers of participation rights for all additions to savings accounts and for all new savings accounts after November 30, 1962. Each member's share account balance or balances as of that date shall be reduced by (1) the amount of any Long Beach share loan as of November 30, 1962 and/or the amount, as shown by the Long Beach books and records, for which each such share account was pledged or assigned, as of November 30, 1962, to any other person, (2) withdrawals from each such account subsequent to November 30, 1962, the last in, first out rule being applied to such withdrawals, and (3) the amount by which the total remaining balance or balances exceeds the sum of (a) $10,000 and (b) the balance or balances, if any, in such member's account or accounts on April 22, 1960.
>
> "This Agreement is not intended to prohibit any shareholder member of Long Beach from taking appropriate action to exercise such rights, if any, which he may have to contest the merits or validity of the plan of dissolution of Long Beach, or any part thereof, incorporated herein.
>
> "Long Beach and Equitable agree that no withdrawals made after the effective date of the Merger shall affect the right of any Long Beach shareholder hereunder as vested on said date, and said shareholders so withdrawing shall participate as fully as if such withdrawal had not been made.
>
> "Each officer and director of Long Beach and Equitable shall participate in the distribution only to the extent of his respective share account as of April 22, 1960 and shall furnish an affidavit to the Federal Home Loan Bank Board to the effect that he is not participating directly or indirectly in the distribution of Long Beach, except to the extent set forth in the proxy Statement.

"Members of the Shareholders' Protective Committee, attorneys representing Long Beach, Equitable or the Shareholders' Protective Committee and close relatives of such persons, and close relatives of officers and directors of Long Beach and Equitable and corporate entities controlled by any of them, shall not participate in the distribution of stock as herein contemplated, except to the extent of the balances of such members' accounts in Long Beach as of April 22, 1960. Close relatives shall be deemed to mean spouses, children, parents, brothers, sisters, nephews, nieces and anyone married to one of the foregoing persons."

Briefly summarized, the distribution provisions denied ticipation rights in the Equitable stock with respect to that tion of new accounts, or additions to April 22, 1960 account ances, in excess of $10,000 and with respect to pledged ounts to the extent of the pledge.[15/] In addition, it restricted ious "insiders" from participating in the distribution except the extent of their April 22, 1960 account balances.[16/] The

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Even Mr. Gregory, in his letter of July 25, 1962 (Exh. C-6), med to concede the fairness of the restriction with respect to dged accounts when he said, "Since the Association [Long Beach] ns, secured by its share accounts are deducted perhaps other ns made on the security of such share accounts should be deted as a matter of equity."

For appellees' account of the background leading to the posit of these large sums see infra, pp. 51-53.

Under the District Court's judgment such "insiders' acquired ticipation rights to the full extent of their account balances, n though Long Beach in its letter of December 2, 1962 to the rd (Exh. C-16) stated, "The participation of the officers and ectors of Long Beach and Equitable in the distribution of the surplus, reserves and undivided profits of Long Beach upon ger with Equitable will be limited to the amounts of their pective accounts in Long Beach as of April 22, 1960, the date Association was seized."

$10,000 figure was selected because it is the maximum amount of federal account insurance; the Board believed that generally new accounts would not be opened by bona fide savers in amounts larg than $10,000 in any one account (McMurray affdvt., 3R 1002).

The Merger Agreement with the restrictive distribution provisions was executed by Long Beach and Equitable on June 12, 196 (Exh. C-52). The Board conditionally approved it on June 14, 19 the conditions being formal and technical (Exh. C-56). The Long Beach management shortly thereafter mailed the proxy statement, including copies of the Merger Agreement (Exh. E), to its membe with its letter dated June 17, 1963 (Exh. C-57). The Long Beach members approved the Merger Agreement overwhelmingly at their meeting on July 6, 1963 (Exhs. C-59, C-59A, C-60). The Equitab stockholders thereafter voted their approval, and the Californi Commissioner granted his approval (Exh. C-64). The Board's fin approval was given on September 5 (Exh. C-67) and on September 1963, the merger was consummated (Exhs. D-1, D-10). To that po no proceedings of any sort had been instituted to enjoin the merger or to test the validity of the approved provisions with respect to the distribution of Equitable stock.

2. Proceedings in the District Court

As set forth above, supra, pp. 3 - 6, the challenge to th tribution terms of the Merger Agreement was initiated immediate after the merger was consummated on September 10, 1963. On October 28, 1963 a stipulation was entered into by the parties

oved by and filed in the District Court on October 29, 1963 orizing distribution of 585,821 of the 791,650 shares of table guarantee stock to those former Long Beach shareholders he extent their accounts were unaffected by the restrictive ribution provisions of the Merger Agreement (3R 167-179). District Court's order effectuating the terms of the stipuon became effective on December 10, 1963 (3R 180-190, 309-311).[17/] ownership of the remaining 205,829 shares is in dispute and he District Court judgments are upheld, these shares, conuting 26% of the total, will be distributed to the speculating stors who for the most part, insofar as the record discloses, acting on the basis of what might be termed "inside information".[18/]

Following the filing of further pleadings in the three ons and after some discovery, as limited by the District t (see footnote 14, supra, p. 13), and an abortive pre- l hearing on May 20-21, 1964 (Tr. 539-581), the District t directed the parties to file cross-motions for summary ment (Tr. 581-606). The motions were filed on June 8, 1964 argued on June 22-23, 1964 (3R 874-1361, 1371-1413; Tr. 613-). The District Court filed its Memorandum Opinion on ember 22, 1964 (1R 553-588; 3R 1477-1512) and its judgments

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Judicial notice may be taken of the fact that the most recent rt, dated July 25, 1966, filed by Equitable in the District t with respect to the stipulated distribution shows that as uly 22, 1966, 465,214 shares, 79.41% of the 585,821 shares, been distributed to eligible former Long Beach shareholders.

See infra, pp. 51-53.

on May 17, 1965 (1R 697-761; 2R 907-971; 3R 1642-1706). The Board and the Insurance Corporation filed their notices of appea on July 9, 1965 (1R 828-829; 2R 1019-1021; 3R 1765-1767). The District Court, on September 8, 1965, denied the motion of the Board and the Insurance Corporation for a stay of the District Court's judgments pending appeal (1R 820-825; 2R 1079-1085; 3R 1838-1844). This Court, by order dated November 18, 1965, granted a stay pending appeal.[19/]

19/ Appellees' petition for an order fixing attorneys' fees wa heard by the District Court on June 23-25, 1965. Its memorandu opinion with respect to this matter was filed on July 25, 1966. A copy thereof is reproduced in the Appendix, pp. 53a - 80a.

3. The District Court Decision

The District Court held:

(a) That the restrictive provisions of the Merger Agreement respect to the distribution of Equitable guarantee stock to Long Beach shareholders were contrary to law, the Long Beach ter and the Settlement Agreement and were therefore a nullity.

(b) That it had the power to change the distribution terms he Merger Agreement and to order pro rata distribution of the table guarantee stock to the Long Beach shareholders.

(c) That the Board had agreed to be, and was, bound by the nent of the District Court and, in any event, since the dis- ution terms of the Merger Agreement were a nullity, the Board no further function to perform.

(d) That the California Savings and Loan Commissioner was ect to suit in the District Court and was bound by the District : judgment.

(e) That the appellees were not estopped from challenging validity of the distribution provisions of the Merger Agreement.

(f) That there was no genuine issue as to any material fact hat the appellees were entitled to judgment as a matter of

4. Statutes and Regulations Involved

(a) Section 5(d)(2) of the Home Owners' Loan Act (12 U.S.C. d)(2)) reads:

"The Board shall have the power to make rules and regulations for the reorganization, merger, and liquidation of Federal associations . . ."

(b) The applicable federal regulation is 12 C.F.R. 546.4 which reads:

"The Board of directors of any Federal association may propose a plan for the dissolution of such association. Such plan may provide for (a) the Federal Savings and Loan Insurance Corporation to be appointed, in accordance with the provisions of Section 406 of the National Housing Act, as amended, and section 5, Home Owners' Loan Act of 1933, as amended, and pertinent regulations of such corporation, as receiver for the purpose of liquidation; (b) all assets of the association to be transferred to another thrift and home-financing institution under Federal or State charter for a sufficient amount of cash to pay all obligations of the association and to retire all outstanding share accounts up to the amount credited thereto; (c) the transfer of all assets to another thrift and home-financing institution under Federal or State charter in consideration of the payment of all outstanding obligations of the association and the issuance of share accounts or other evidence of interest to the members of the Federal association on a pro rata basis; or (d) dissolution in such other manner as may be proposed by the directors and which to them appears to be to the best interest of all concerned. Such plan shall thereupon be submitted to the Board for approval, together with a statement of the reasons for proposing dissolution and the reasons for the plan submitted. If it appears to the Board that dissolution is advisable and that the plan of dissolution submitted is in the interest of all concerned, the Board will approve the plan; if the plan submitted appears to be inadvisable, the Board will either make recommendations to the association concerning the plan or disapprove it. When a plan of dissolution has been approved by the board of directors of a Federal association and by the Board, such plan shall be submitted to

the members of such association at a duly called meeting and, when approved by a majority of the votes cast at such meeting, shall become effective. When dissolution has been consummated in accordance with the plan approved by the Board, a certificate evidencing that fact, supported by such evidence as the Board may require, shall forthwith be filed with the Board. Upon receipt of evidence satisfactory to the Board that such dissolution has been so consummated, the Board will terminate the corporate existence of the dissolved Federal association and its charter shall thereby be cancelled." (Emphasis supplied)

(c) The applicable California statutes are incorporated in the following sections of the California Financial Code relating to Savings and Loan Associations:

Section 9203: MERGER AND CONSOLIDATION OF DOMESTIC AND FEDERAL ASSOCIATIONS.
Any one or more domestic associations, and any one or more federal savings and loan associations, may be merged into one of such constituent associations or consolidated into a new association, domestic or federal, with or without any dissolution or division of the funds or property of any of them.

Section 9204: TRANSFER OF ENGAGEMENTS, FUNDS, AND PROPERTY TO FEDERAL ASSOCIATION: RATIFICATION OF AGREEMENT BY STOCKHOLDERS AND SHAREHOLDERS.
. . . any federal savings and loan association may transfer its engagements, funds, and property, in whole or in part, to any domestic association, upon such terms as may be agreed by the affirmative vote of at least a majority of their respective directors, ratified, in the case of the contracting domestic association by the vote or written consent of stockholders holding in the aggregate more than two-thirds of the outstanding stock and by the vote or written consent of shareholders holding in the aggregate more than two-thirds in value of the outstanding shares, and in the case of a contracting federal

savings and loan association by the consent, in writing or by vote, prescribed by the laws of the United States and the regulations of the Federal Home Loan Bank Board applicable thereto.

Section 9205: APPROVAL OF COMMISSIONER; COMPLIANCE WITH FEDERAL LAW.
Any merger, consolidation, or transfer made pursuant to Sections 9203 and 9204 shall be approved by the commissioner, and with respect to any constituent domestic association be made in conformity with the provisions of law applicable to mergers, consolidations, and transfers in the case of corporations generally, and with respect to any constituent federal savings and loan association, be made in conformity with the provisions of the laws of the United States, and the rules and regulations of the Federal Home Loan Bank Board applicable to mergers, consolidations and transfers.

5. Specification of Errors

The District Court erred:

(a) In holding that it had the power to change the distril terms of the Merger Agreement and to order distribution of the Equitable guarantee stock to the Long Beach shareholders on a p rata basis (3R 1803).

(b) In failing to hold that appellees should have sought junctive relief prior to the consummation of the merger (3R 180

(c) In holding that the distribution terms of the Merger ment with respect to the Equitable guarantee stock were null an void (3R 1803).

(d) In failing to find that the officers and directors of Beach breached their fiduciary responsibilities to their shareh

ncouraging and permitting the large influx of speculative ounts into Long Beach on and after April 2, 1962 (3R 1803).

(e) In failing to uphold as valid and reasonable the dis- bution terms of the Merger Agreement as approved by the Board the California Commissioner (3R 1803, 1804).

(f) In failing to dismiss the actions on the ground that California Commissioner was an indispensable party who was subject to suit in the District Court (3R 1803).

(g) In limiting the Board's right of discovery with respect scertaining account activity at Equitable after consummation he merger on September 10, 1963 with respect to those former Beach shareholders whose participation rights to Equitable antee stock were restricted by the distribution terms of the er Agreement (3R 1803).

(h) In holding that the Shareholders' Protective Committee uately represented those Long Beach shareholders unaffected he restrictive distribution terms of the Merger Agreement adversely affected by the District Court's judgments (3R 1803).

(i) In granting summary judgment against the Board and the rance Corporation and in favor of the appellees (3R 1804).

(j) In failing to grant summary judgment for the Board and Insurance Corporation (3R 1804).

SUMMARY OF ARGUMENT

I. The District Court undertook to reform a Merger Agreem which had been previously approved by all the necessary parties as well as by the Federal Home Loan Bank Board and the Californ Savings and Loan Commissioner, as required by federal and state law. The District Court had no power to rewrite the Merger Agr ment, and to by-pass the regulatory agencies which alone were empowered by federal and state legislative bodies to regulate mergers of savings and loan institutions.

II. The only relief available to the aggrieved shareholde of Long Beach was to enjoin the merger. Although fully advised of the intent to merge months in advance of the actual consumma the aggrieved shareholders waited until the consummation took p to file their actions. At that time the only remedy available an action to set aside the merger, but even if the present comp could be so construed, the aggrieved shareholders are barred by laches, they having with full knowledge of the facts delayed fi suit to the prejudice of many innocent parties.

III. The Merger Agreement, in all events is valid. The charter provision upon which the District Court relies relates liquidation, dissolution or winding up of the Association, and vides that in such event the net assets shall be distributed pr rata. The merging of Long Beach with Equitable, a state saving and loan association, is not a liquidation, dissolution or wind up of the association, and the authorities so hold. Even if th

rary were true, the Merger Agreement would be valid if it e found by the Court to be fair -- though in conflict with charter. The merger provisions here under attack were designed to exclude from participation in the distribution of itable stock last minute speculators who had contributed ing to the establishment of Long Beach's net worth as a ng concern.

IV. The California Savings and Loan Commissioner by state is required to pass upon and approve all mergers of state ngs and loan associations. Therefore, he is an indispensable y to any action attacking a merger subject to his control. California Commissioner is not subject to the jurisdiction ne federal District Court in these proceedings, and the ons should have been dismissed because of the absence of an spensable party.

ARGUMENT

I. THE DISTRICT COURT HAD NO POWER TO CHANGE THE DISTRIBUTION TERMS OF THE MERGER AGREEMENT AND, AS APPELLEES REQUESTED, TO ORDER DISTRIBUTION OF EQUITABLE STOCK ON A PRO RATA OR ANY OTHER BASIS.

A. The Governing Statutes and Regulations

Notwithstanding that none of the parties contended below that ion 5(i) of the Home Owners' Loan Act of 1933, as amended (12 C. 1464(i)), was applicable, the District Court, without the fit of any briefing or argument, concluded that, in the ution and implementation of the Merger Agreement, "the Board

and the Association were proceeding under the provisions for merger and dissolution by vote of the shareholders [second un-numbered paragraph of 12 U.S.C. 1464(I)], which does not requi approval of the Board [Federal Home Loan Bank Board v. Greater Delaware Valley Federal Savings & Loan Association, et al. (3rd Cir., 1960) 277 F. 2d 437], and not under the provisions set fo in the third unnumbered paragraph of that subsection upon such 'equitable' basis as may be approved by the Bank Board." (233 F. Supp. at p. 592). The District Court was plainly in error i so concluding.

In the first place, as the lower and appellate court opini in the very case cited by the District Court in reaching its erroneous conclusion show, Section 5(i) of the Home Owners' Loa Act deals, not with mergers, but with conversions. Federal Hom Loan Bank Board v. Greater Delaware Valley F. S. & L. Ass'n., F. Supp. 24 (E.D. Pa., 1959), aff'd. 277 F. 2d 437 (3rd Cir., A merger, as in the instant case, involves two or more entitie a conversion relates solely to one entity, the charter of whic being changed either from federal to state or state to federal the second place, as the lower court opinion in Greater Delawa Valley makes clear, the second unnumbered paragraph of Section with respect to which Board approval is not required, relates conversion from a federal *mutual* to a state *mutual* association

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20/ The 6th proviso of the second unnumbered paragraph of Sec 5(i) reads: "(6) that, in the event of dissolution after conve the members or shareholders of the association will share on a basis in the assets of the association in exact proportion to relative share or account credits."

5 F. Supp. at pp. 29, 32). Here, even if conversion were etched to include mergers, the "conversion" would have been m a federal mutual into a state stock association, the latter ng the resulting or surviving institution. Since the saver-bers in a stock association do not participate on a mutual is with the stockholders, as the 6th proviso of the second umbered paragraph of Section 5(i) demands, such a "conversion" ld have been effected only under the third unnumbered paragraph Section 5(i), "upon an equitable basis" and with Board approval. eral Home Loan Bank Board v. Greater Delaware Valley F. S. & L. 'n., 176 F. Supp. at p. 32. See 12 C.F.R. 546.5 for the licable Board regulation in this area. In short, Section 5(i) the Home Owners' Loan Act has no application here, and if it , the third unnumbered paragraph of that Section would have lied under which the Board would have had to approve the "con-sion" after finding that it was on an equitable basis.

The governing federal statute, as to which there was no pute below and which was never mentioned in the District Court nion, is that portion of Section 5(d)(2) of the Home Owners' n Act (12 U.S.C. 1464(d)(2)) which reads:

> "The Board shall have the power to make rules and regulations for the reorganization, merger, and liquidation of Federal associations . . ."

The applicable federal regulation, as to which again there s no dispute below and which again was never mentioned in the

District Court opinion, is 12 C.F.R. 546.4 cited in full (*infra* pp. 20 - 21) provides in part, as follows:[21/]

> "The Board of directors of any Federal association may propose a plan for the dissolution of such association. Such plan may provide for . . . (d) dissolution in such other manner as may be proposed by the directors and which to them appears to be to the best interest of all concerned. Such plan shall thereupon be submitted to the Board for approval, together with a statement of the reasons for proposing dissolution and the reasons for the plan submitted. If it appears to the Board that dissolution is advisable and that the plan of dissolution submitted is in the interest of all concerned, the Board will approve the plan; if the plan submitted appears to be inadvisable, the Board will either make recommendations to the association concerning the plan or disapprove it. . ."

While the District Court made no mention of California law §§ 9203 and 9204 of the Financial Code (*infra*, p. 21) authoriz mergers between a federal association and a California-chartere stock association, if authorized by a majority of the directors and if approved by holders of more than two-thirds of the outstanding stock of the state association. In addition, under Section 9205 (*infra*, p. 22), such mergers must be approved by t appellant California Commissioner.

21/ The Board then had no regulations explicitly applicable to merger between a federal association and a state-chartered insti tution where the *latter* is to be the resulting or surviving association. See 12 C.F.R. 546.1 - 546.3 (Rev. as of January 1 1963). It was for that reason that 12 C.F.R. 546.4 was employe by the Board and by Long Beach as the regulatory channel throug which the instant merger was processed.

The procedures prescribed by the applicable federal and state ı, as set forth above (supra, pp. 20-21), were followed here. ı Long Beach management submitted to the Board for approval, ısuant to and in accordance with 12 C.F.R. 546.4 (Exh. E, p. 46, (. C-2, p. 3), the Merger Agreement which had been executed by ı duly authorized officers of Long Beach and Equitable and which ɔtained the distribution provisions struck down by the District ɔrt. The Board granted its approval of the Agreement as sub-ıted and the Long Beach members thereafter overwhelmingly voted ıir approval of the same. Similar action with respect to the (cuted Merger Agreement was taken pursuant to California law by ı Equitable management, the Equitable stockholders and the ıifornia Commissioner.

B. The District Court Action was Taken Without Obtaining The Necessary Approvals

Notwithstanding the controlling statutes and regulations, the ıtrict Court did not limit itself to declaring null and void the ıegedly illegal distribution terms of the Merger Agreement and ıting such relief, if any, as would have been appropriate in ıt of such statutes and regulations. On its own, it revised ı Merger Agreement. This it did by in effect striking therefrom ı distribution terms which had received the approval of the ıeral and state supervisory authorities and of the Long Beach ıbers and Equitable stockholders, and substituting for such terms ıvision for a pro rata distribution which had not received the

supervisory and other approvals required by statute and regulat
Having thus reformed the Merger Agreement to its liking, the Dis
Court proceeded to order distribution of the Equitable stock in
accordance with its revisions.

Manifestly, the District Court had no power to disregard th controlling statutes and regulations. With respect to the appe Board, Congress in Section 5(d)(2) of the Home Owners' Loan Act delegated to the Board, and not to the courts, the power to regu late mergers. Under the applicable regulation (12 C.F.R. 546.4) the approval of the Board is an essential prerequisite to the effectuation of a merger. Though the courts may in appropriate circumstances determine the legality of provisions of a particu merger agreement, they are not empowered to supply the necessary administrative actions by way of approval or disapproval. As th Supreme Court has said in S.E.C. v. Chenery Corp., 318 U.S. 80, (1943):

> ". . . if an order is valid only as a determination of policy or judgment which the agency alone is authorized to make and which it has not made, a judicial judgment cannot be made to do service for an administrative judgment. For purposes of affirming no less than reversing its orders, an appellate [or trial] court cannot intrude upon the domain which Congress has exclusively entrusted to an administrative agency."

The Supreme Court on a later occasion articulated the fore going principle as follows (Aircraft & Diesel Equipment Corp. v. Hirsch, 331 U.S. 752, 767 (1947)):

> "Where Congress has clearly commanded that administrative judgment be taken initially or exclusively, the courts have no lawful function to anticipate the administrative decision with their own . . . . To do this not only would contravene the will of Congress as a matter of restricting or deferring judicial action. It would nullify the congressional objects in providing the administrative determination."

See also Schwabacher v. United States, 334 U.S. 182 (1948); ...y v. Powell, 314 U.S. 402 (1941); FTC v. Pacific Power & Light ..., 307 U.S. 156, 160 (1939); Mississippi Valley Barge Line Co. ... United States, 292 U.S. 282 (1934); Greater Delaware Valley ...ral S&L Ass'n. v. Federal Home Loan Bank Board, 262 F. 2d 371, 4 (3rd Cir., 1958).[22]

C. The Necessary Administrative Approvals to the District Court's Formula Were Not Supplied Either in the Approved Merger Agreement or in The Settlement Agreement of February 14, 1962.

1. The District Court seemed to take the position in its ...ion (233 F. Supp. at pp. 594, 596-7) that the Board granted ...s necessary approval to the Court's revised "agreement" because ...he following provision in the approved Merger Agreement (Exh. ..., 47):

> "This agreement is not intended to prohibit any shareholder member of Long Beach from taking appropriate action to exercise such

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[22] The same principles would necessarily govern with respect to ...e approvals of the California Commissioner and of the Long Beach ...ners and Equitable stockholders in connection with the District ...t's revised merger "agreement".

rights, if any, which he may have to contest the merits or validity of the plan of dissolution of Long Beach, or any part thereof, incorporated herein." 23/

It is difficult to understand how the foregoing provisions could be construed by anyone as an abandonment by the Board of its statutory and regulatory responsibilities and the delegatio of such duties to the courts. In the first place, the Board (though implicitly approving the existence of this particular provision by approving the Merger Agreement as a whole) was not a party to the Agreement. It is no more contractually bound by quoted provision than by the many other provisions of the Merge Agreement. Secondly, the provision is nothing more nor less th a restatement of the law. The most that it says is that the co tracting parties (Long Beach and Equitable) have made no agreem which would prohibit any aggrieved Long Beach shareholder from exercising such rights as he may have (and he may have none) to contest the validity of the Agreement or any part thereof. Any aggrieved shareholder would, of course, have had such right eve in the absence of such a provision. The provision likewise cou not alter existing law as to the extent and manner of exercise a shareholder's rights or the relief to which he might be entit Thirdly, even if the Board had intended to be bound contractual

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23/ This provision was inserted in the Merger Agreement at the request of the Shareholders' Protective Committee and Long Beac and not, as the District Court seems to suggest (233 F. Supp. a p. 596), at the Board's request. See appellees' proposed findi 42 (3R 1203).

the provision and the provision could reasonably be read as a egation by the Board to the courts of its administrative ies and responsibilities in this regard, such delegation would e been a nullity. See Mississippi Valley Barge Line Co. v. ted States, 292 U.S. 282 (1934).[24/]

2. Nor does the Settlement Agreement of February 14, 1962 e any application here. It is true that Article XV of that eement (Exh. 8, pp. 43-48) contained the Board's approval[25/]

/ A so-called memorandum of understanding from Mr. McMurray, Board Chairman, to Mr. Gregory, President of Long Beach, ed May 30, 1963 (Exh. C-44) makes it abundantly evident that Board was not abdicating its responsibilities. That memodum, so far as pertinent here, reads:

> "For your information, it is the Board's position that, insofar as it is concerned, no Long Beach Shareholder who abstains from voting on the plan at the meeting of Long Beach members will be prejudiced in any way by such abstention in the event action should be instituted against the Board, et al. attacking the validity or merits of the plan, in whole or in part. The Board will otherwise employ every legal defense available to it to defend the plan's validity and its merits. The Board believes that, since the plan will have been proposed by the management of Long Beach, and approved by Long Beach members, Long Beach Federal will necessarily have to defend the plan or take a neutral position. To do otherwise would be inconsistent with the action of its management and with the vote of its members approving the plan." (Emphasis supplied)

/ The Settlement Agreement does not, of course, in any way inle the appellant California Commissioner or constitute his oval of anything.

of the liquidation plan specifically described therein, a plan which did provide for a pro rata cash distribution of Long Beac surplus. As will be shown below, Board approval was granted on for that plan and, more specifically, no Board approval was gra in the Settlement Agreement for a merger between Long Beach and Equitable requiring pro rata distribution of stock received fro the surviving association.

The District Court at several points in its opinion equate the Article XV liquidation plan to a merger between Long Beach Equitable (233 F. Supp. at pp. 584, 585, 586, 594) and seemed t conclude that pro rata distribution was therefore required. An examination of Article XV demonstrates that there is no merit i the Court's supposition.

The Article XV liquidation plan provided for the transfer Long Beach savings accounts to Equitable which, in turn, was to assume liability therefor. In consideration of such assumption of liability, Long Beach was to transfer to Equitable an equal amount of Long Beach assets. The remaining assets of Long Beac after payment or provision for payment of creditor claims, were to be distributed, either directly by Long Beach or through a trust, to Long Beach shareholders on a pro rata basis. Obvious this approved liquidation plan was far different from the consummated merger between Long Beach and Equitable. Under the merger, all, and not part, of Long Beach assets and liabilities were transferred to Equitable. Long Beach shareholders, under

merger, were to receive payment for Long Beach's value as a ong concern, not from the proceeds of the liquidation of Long ach assets, but by way of the distribution of Equitable guarantee ck to them. These are the principal differences in the two ns; see Exhibits C-21, C-22, C-26, C-30, C-33, C-34, C-35, C-50 a detailed listing of other differences.

Again, if the Article XV liquidation plan, already approved the Board, were indeed the same as a merger between Long Beach Equitable, Long Beach would not have sought Board approval of merger and spent from May 1962 to June 1963 negotiating with Board with respect to the terms of the merger. Yet, this is ecisely what it proceeded to do. And the fact of the matter is Long Beach, in the last paragraph of Article XVII of the ger Agreement, expressly recognized that the Merger Agreement not an implementation of the Article XV liquidation plan but alternative to it (Exh. E, p. 51).26/

/ This paragraph reads:

"Each Association does hereby reserve, pending consummation hereof, all rights and agreements between the parties pertaining to carrying out the purposes and intent of Article XV of that certain Settlement Agreement made between the Federal Home Loan Bank Board, Federal Savings and Loan Insurance Corporation and Long Beach Federal Savings and Loan Association dated February 14, 1962, and each Association specifically agrees that in the event, for any reason, the within Merger Agreement not be consummated, that each Association shall be bound by the agreements between the Associations pertaining to said Article XV and shall exert every effort to consummate the same."

Finally, it must be remembered that Long Beach was not contractually, or otherwise, bound to follow the Article XV plan. It had the right to do so, if it so chose. But, apparently believing that the merger route was preferable to the liquidation plan, for tax and other reasons, it voluntarily chose the forme Plainly once the Article XV liquidation plan was abandoned by Long Beach, as it had a right to do, and the merger plan propos the Board had the statutory and regulatory duty to examine into all existing facts, terms and circumstances to determine whethe and on what basis the merger should be approved. Those facts a circumstances (supra, pp. 9-11) had changed markedly since the execution of the Settlement Agreement. They disclosed a rapid abnormal increase in large savings accounts resulting from inve ments by persons with no prior account holder connection with L Beach and under circumstances plainly establishing a breach of fiduciary duty by the Long Beach management. This influx of la accounts into Long Beach only served to dilute the interests of the other Long Beach shareholders. Because of these changed ci cumstances, the Board, to effectuate its statutory and regulato responsibilities, could have either rejected the merger as unfa and inequitable under the prevailing circumstances or approved upon the basis of a different and equitable formula which provi for the distribution of Equitable stock on other than a pro rat basis. It chose the latter course of action, and both associat presented that plan to their shareholders and the California

missioner for approval. Manifestly, the District Court was in rr in its seeming assumption that the pro rata provision of the adoned liquidation plan had to be accepted by the Board, either matter of contract or Board policy, in its consideration of e new merger plan.

II. <u>IN THE CIRCUMSTANCES OF THIS CASE, THE AGGRIEVED LONG BEACH SHAREHOLDERS, NOT HAVING SOUGHT TO ENJOIN CONSUMMATION OF THE MERGER, ARE NOT ENTITLED TO ANY RELIEF.</u>

A. <u>The Only Conceivable Relief to Which The Aggrieved Long Beach Shareholders Might Be Entitled Is To Set Aside The Merger.</u>

Case and text book authorities describe four possible remedies ilable to aggrieved shareholders in respect of an allegedly il- gl merger: (1) damages for conversion; (2) appraisal rights; enjoining the merger; and (4) setting aside the merger. <u>lantine on Corporations</u> (rev. ed., 1946), §§ 295 et seq. and s there cited; 15 <u>Fletcher, Corporations</u> (rev. ed., 1961, §§ -7167 and cases there cited; see also 4 <u>Pomeroy</u>, Equity (5th 1941), § 1093.

Relief by way of damages for conversion runs against the essor corporation. <u>Lebold</u> v. <u>Inland Steel Co.</u>, 125 F. 2d 369 Cir., 1941), mod. 136 F. 2d 876 (1943); <u>American Seating Co.</u> <u>ullard</u>, 290 F. 896 (6th Cir., 1923); <u>Finch</u> v. <u>Warrior Cement Co.</u>, el. Ch. 44, 141 A. 54 (1928); <u>Wunsch</u> v. <u>Consolidated Laundry Co.</u>, Wash. 44, 198 P. 383 (1921); <u>Garrett</u> v. <u>Reid-Cashion Land &</u>

Cattle Co., 34 Ariz. 245, 270 P. 1044 (1928); Friedman v. South Co-op. Building & Loan Ass'n., 104 Pa. Super. Ct. 514, 159 A. (1932). The instant complaints cannot be read as asserting cau of action against Equitable for conversion, and appellees have requested such relief.

With respect to appraisal rights, this is a statutory reme as to which there is no applicable federal statute. Moreover, while California law as to appraisal rights was made applicable by the Merger Agreement to certain Long Beach shareholders, suc rights were specifically withheld from those adversely affecte by the distribution provisions. See Section 3 of Article VIII Merger Agreement (Exh. E, p. 48). Moreover, the complaints do not state a cause of action with respect to appraisal rights ar the appellees do not request such relief.

The merger having been consummated on September 10, 1963, relief by way of enjoining the merger is now too late. As wil be shown in point "B", infra, this relief was available to but apparently deliberately, not utilized by the appellees.

Thus, the only conceivable remedy available to aggrieved shareholders in the circumstances is to set aside the merger, the complaints can be read as stating a cause of action for the granting of such relief. While the appellees have not specifi requested such relief, such a request can be read into their ge

ver for appropriate relief.[27/]

B. Laches Bars Relief by Way of Setting Aside the Merger.

Even if appellees should request that the merger be set aside, laches, it is submitted, bars such relief. The doctrine of laches, the area of mergers, has been stated in the following language 9 Am. Jur. 2d, Corporations, § 1544, p. 900):

> "A stockholder who has the right to object to a consolidation, merger, reorganization, or sale of the corporate assets may lose this right by laches, where, with knowledge of the facts, he has delayed the assertion of his rights until the rights of third persons have intervened, or the defendants have expended money or incurred liabilities in reliance on the complainant's apparent acquiescence in what has been done, or it would be inequitable for any reason to grant the relief sought."

The elements of laches are thus (1) full knowledge of the cts, (2) delay, and (3) prejudice to the opposing party or t'rvening rights of third parties or other inequity. All eents are present here.

All Long Beach shareholders, including the appellee members he Shareholders' Protective Committee, were on notice of all

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/ The granting of such relief, were it now appropriate, would ire Equitable to be divested of Long Beach assets and liabilities association would then be in a position to negotiate and execute w merger agreement for submission to their respective shareholder stockholders and to the federal and state supervisory authorities the necessary approvals, or to continue their respective business ations if no new agreement were forthcoming.

the material facts with respect to the merger after the mailing of the proxy statement in the middle of June 1963 (Exhs. C-57, As of that time, the Merger Agreement, containing the allegedly illegal distribution terms, had been executed by Long Beach and Equitable and had been conditionally approved by the Board (Exh C-56). The Merger Agreement, as executed, was an integral part of the proxy statement, and the proxy statement referred to the possibility that litigation might be commenced in respect of th distribution provisions of the Merger Agreement (Exh. E, p. 5). Thus, the Long Beach shareholders, including the Shareholders' Protective Committee, had an opportunity from the middle of Jun 1963 until September 10, 1963, to challenge the allegedly ille distribution provisions by seeking to enjoin the consummation o the merger. Instead the Shareholders' Protective Committee, wh purports to represent all Long Beach shareholders[28/] apparently d erately refrained from exercising the aggrieved shareholders' rights to test the validity of the distribution provisions by v

28/ The attorney for Long Beach, rather than counsel for the Shareholders' Protective Committee, has played the most active role in the conduct of this litigation.

injunction. They obviously wanted the merger to be consummated ter than enjoined since their two complaints, necessarily pre-d in advance, were filed in the federal and state courts the r day the merger was consummated. Certainly on these undisputed s the element of knowledge is present.

As to delay, it has been held that a delay of a month or less ufficient to give rise to the defense of laches. Andrews v. eision Apparatus Inc., 217 F. Supp. 679 (S.D. N.Y., 1963); nhurst v. Central Leather Co., 101 N.J. 543, 138 A. 772 (1927). r the delay was almost three months, a seemingly unconscionable m in the circumstances.

With respect to the third element, prejudice has been held xist and the defense of laches available where a merger has e consummated, assets intermingled, and third parties have tined rights to the stock of the successor corporation. tonal Supply Co. v. Leland Stanford Jr. University, 134 F. 2d 9 (9th Cir., 1943), cert. den. 320 U.S. 773 (1943); Katz v. R. e & Co., Inc., 278 App. Div. 766, 104 N.Y.S. 2d 14 (1st Dep't.,), 342 U.S. 886 (1951); Windhurst v. Central Leather Co., supra; ing v. American Tobacco Co., 72 N.J. Eq. 32, 65 A. 725 (Ch.,); Dana v. American Tobacco Co., 72 N.J. Eq. 44, 65 A. 730 (Ch.,), aff'd. 73 N.J. Eq. 736, 69 A. 223 (Ct. Err. & App., 1908), a nanion case to Beling; see also Fraser v. Great Western Sugar Co., A. 60 (N.J. Ch., 1935), aff'd. 185 A. 64 (Ct. Err. & App., 1936). in one case it has been held that even if it might be possible estore the status quo ante, the difficulty and inconvenience

should not devolve upon a defendant corporation due to the dela[y of] a stockholder in bringing suit. Union Financial Corp. of Ameri[ca v.] United Investors' Securities Corp., 156 A. 220 (Del. Ch., 1931)[. In] other words, it is not necessary that the process of unscrambli[ng] merged corporate entities be an impossible or extremely difficu[lt] task. Finally, see Federal United Corp. v. Havender, 11 A. 2d [331] (Del. Sup. Ct., 1940), in which the court stated avoidance of laches in terms of duty (p. 343):

> ". . . where many persons will be affected by an act that involves a change of capital structure and a material alteration of rights attached to stock ownership, the stockholder, having knowledge of the contemplated action, owes a duty both to the corporation and to the stockholders to act with the promptness demanded by the particular circumstances."

In our case the prejudice involved, if the merger were to [be] set aside, is obvious. By reason of the non-appealable consent order of October 29, 1963, requiring distribution of the Equita[ble] stock not in dispute, the rights of Long Beach shareholders receiving such stock[29] would be seriously prejudiced in the event [the] merger were to be set aside. In addition, purchasers of Equita[ble] stock since the merger would be affected. The assets of Long Beach and Equitable have been intermingled and the unscrambling

29/ 465,214 shares of stock have been distributed as of July 2[?], 1966. See footnote 17, supra.

ereof would pose serious problems, particularly in light of the
c that Equitable has been operating as a successor entity for
ost three years. The supervisory authorities would also be
ely involved in and burdened by any unscrambling. The Board
ld be concerned about protection of the interests of Long Beach
reholders and the California authorities would be concerned
ut protection of Equitable.

Indeed, appellees' position is generally lacking in equity,
hat it appears that they have maneuvered both to have their
ger and also to undo the basis upon which it was approved by
ervisory authority, both state and federal. The dilemma with
h they have thus confronted the Court is of their own
lberate construction.

If this Court agrees with appellants' contention that the
remedy now available to the appellees is the setting aside
he merger, the consequence of which would be the divesting
quitable of Long Beach assets and liabilities, and further
res that this remedy is in the circumstances present here
red by laches, such holdings would be dispositive of the
pals, and the District Court should be directed to dismiss
e actions and return the impounded stock for distribution in
ordance with the provisions of the Merger Agreement. Only if
e Court disagrees need it consider appellants' additional
gments.

III. IN ANY EVENT, THE DISTRIBUTION TERMS OF THE MERGER AGREEMENT ARE VALID

A. The Long Beach Charter Does Not Require Pro Rata Distribution in the Case of a Merger

The District Court held (233 F. Supp. at p. 552):

> "I am satisfied that and hold that the Officers and Directors of the Association and the Bank Board, or either of them, or the majority of the shareholders did not have the lawful power to alter the pro rata rights of shareholders from that set forth in the law, the charter, and the Settlement Agreement, and that the provisions of the Merger Agreement which attempt to do so are void."

We have shown, supra, pp. 25-29, that the distribution te of the Merger Agreement are not governed by the provisions of Section 5(i) of the Home Owners' Loan Act of 1933, as amended (U.S.C. 1464(i)), 30/ or by Article XV of the Settlement Agreement. shall show here that they are not violative of the Long Beach charter.

The last sentence of Section 9 of the Long Beach charter (19, p. 6) provides:

> "All holders of share accounts shall be entitled to equal distribution of net assets, pro rata to the value of their share accounts, in the event of voluntary or involuntary liquidation, dissolution or winding up of the association."

30/ It is assumed that the District Court's holding that the M Agreement violated "law" was in reference to its discussion of applicability of Section 5(i) of the Home Owners' Loan Act of 1 as amended, to the instant case.

The question then is whether a merger is a "liquidation, solution or winding up" within the meaning of Section 9 of e Long Beach charter. In this connection, Section 3 of the ater empowered Long Beach "to wind up and dissolve, merge, olidate, or reorganize in the manner provided by law and ls and regulations made thereunder; . . ." The omission of e words "merger" or "merge" from Section 9 was not, as the e of the word "merge" in Section 3 makes manifest, accidental ithout significance.

Section 9 was obviously aimed at a situation where a federal ciation wished to terminate its business through liquidation. hat event the charter required that, after payment of its itor claims, the association's remaining assets be distributed ts shareholders on a pro rata basis. A merger, on the other n, does not involve liquidation and distribution of an ciation's assets. Its assets and liabilities are simply sferred to another association which carries on the disappear- g association's business under the resulting association's name d charter.

Whether, in the case of a merger, shareholders of the dis- aring federal association receive any consideration other than e assumption by the resulting association of liability for their ngs accounts depends on all the facts and circumstances sur- nding the merger. Thus, a merger between a federal association, h is a mutual institution, and another mutual association,

federal or state, would not involve the "distribution of net assets" by the resulting or surviving association.[31/] Yet the District Court's holding, by reading the word "merger" into Section 9 of the Long Beach charter, would seemingly require a payment in cash or some other "distribution of net assets" by the resulting association to the disappearing federal association's shareholders in connection with their interests in the disappearing association's net worth. Such a requirement could effectively prevent mergers of mutual associations, notwithstanding that the public interest might call for such action.[32/]

31/ The Supreme Court, in Society for Savings v. Bowers, 349 U. 143, 150 (1955), has described a depositor's (saver's) interest a mutual institution in the following language:

> "The asserted interest of the depositors is in the surplus of the bank, which is primarily a reserve against losses and secondarily a repository of undivided earnings. So long as the bank remains solvent, depositors receive a return on this fund only as an element of the interest paid on their deposits. To maintain their intangible ownership interest, they must maintain their deposits. If a depositor withdraws from the bank he receives only his deposits and interest. If he continues, his only chance of getting anything more would be in the unlikely event of a solvent liquidation, a possibility that hardly rises to the level of an expectancy. It stretches the imagination very far to attribute any real value to such a remote contingency, and when coupled with the fact that it represents nothing which the depositor can readily transfer, any theoretical value reduces almost to the vanishing point."

32/ Any requirement that the net worth of a federal associatio must be distributed to its shareholders in the event of a merge with another mutual association means in effect that the result or surviving association would receive no reserves to absorb lo on the disappearing association's loan portfolio. Since the re sulting association's reserves might not be sufficiently large assume the risk of losses on the assets it would acquire upon m the resulting association and/or the supervisory authorities mi in such circumstances be forced to turn down the merger.

A merger, on the other hand, as here, of a solvent federal ciation into a guarantee stock type association (which is d by its stockholders and not its savings account holders) d necessarily involve a payment by the stock association to shareholder owners of the disappearing federal association. payment, however, would not be made because of the Section arter provision upon which the District Court relied. The utory and regulatory provisions referred to under Point IA, a, pp. 25-29, would require such a payment. The amount and of the payment would necessarily depend upon all the facts circumstances. In this case, the merging parties agreed upon, the supervisory authorities approved, a payment in the form uarantee stock of the resulting surviving entity, Equitable.

The judicial decisions in the area of corporate law are in rd with our position that a charter provision such as that of ion 9 Long Beach charter provision does not control with respect merger. Thus, in Windhurst v. Central Leather Co., 149 A. aff'd. 153 A. 402 (N.J., 1930); Adams v. United States Dis-uting Corp., 34 S.E. 2d 244 (Va., 1945); Anderson v. Cleveland-fs Iron Co., 87 N.E. 2d 384 (Ohio, 1948), it was held that a er was not a dissolution or a liquidation within the meaning he applicable corporate charter. In the Anderson case, pre-ed shareholders sought to prevent the consolidation of two orations on the ground that the plan of consolidation would ive them of their charter rights. The charter provided for

payment of certain sums to preferred shareholders in the event "dissolution, liquidation or winding up of the corporation", an under the proposed plan these payments would not be made. In f one of the objects of the merger was to escape the arrearage in preferred stock dividends. The Court, after analyzing the basi differences between liquidation and merger, ruled that only whe there is a cessation of business and economic functions of the corporation is there any occasion to distribute the assets in t manner described in the charter, and concluded (87 N.E. 2d at p. 396), "In the opinion of the Court the consolidation did not ef 'dissolution' of the defendant corporation within the meaning o that term as used in the liquidation clause of the shareholders contracts." See also <u>Otis & Company</u> v. <u>S.E.C.</u>, 323 U.S. 624 (19 <u>Langfelder</u> v. <u>Universal Laboratories, Inc.</u>, 68 F. Supp. 209 (D. 1946), aff'd. 163 F. 2d 804 (3rd Cir., 1947); <u>Anderson</u> v. <u>International Minerals & Chemicals Corp.</u>, 295 N.Y. 343, 67 N.E. 2d 5 (1946).

B. <u>Assuming Arguendo, That There is a Conflict Between the Distribution Terms of the Merger Agreement and the Long Beach Charter, the Merger Terms, if Fair, Must Prevail.</u>

1. <u>The Board's statutory and regulatory powers are part of the Long Beach charter.</u>

It is an axiomatic principle of corporate law that all stat and constitutional provisions form part of a charter. <u>Fletcher Corp.</u> (1963 Ed.), § 164. Indeed, the Long Beach charter itself

ides in Section 3 thereof, ". . . the association shall exercise powers in conformity with the Home Owners' Loan Act of 1933 and laws of the United States as they now are, or as they may here- r be amended . . ." Thus, all Long Beach shareholders were on ce of the Board's statutory and regulatory powers with respect ergers as set forth in Section 5(d)(2) of the Home Owners' Act of 1933, as amended (12 U.S.C. 1464(d)(2)).[33/] They were on notice that Board approval was required with respect to merger involving a federal association. The controlling regu- on[34/] so provided; under it, the Board had to find the proposed er plan to be "in the interest of all concerned" before ould grant its approval. As stated above, supra, p. 27, District Court did not once allude to the controlling statute egulation.

/ The statute's text is set forth on p. 20, supra, and has so since its amendment by the Act of August 2, 1954, c. 649, e V, § 503, 68 Stat. 636. Prior thereto the statute read,

> "The Board shall have full power to provide in the rules and regulations herein authorized for the reorganization, consolidation, merger, or liquidation of such associations. . ." Act of June 13, 1933, c. 64 § 5(d), 48 Stat. 133.

/ The full text of this regulation is set forth on pp. 20-21, a. A comparable regulation has been in effect since June 1935, r to the issuance to Long Beach of the charter involved here.

2. <u>As between merger terms and charter provisions the merger terms prevail, if fair.</u>

Another well-established principle of corporate law is that the elimination of a charter right under the terms of a merger does not violate a stockholder's legal or constitutional rights, provided the merger meets the test of fairness.[35/] <u>Clarke</u> v. <u>Gold Dust Corp.</u>, 106 F. 2d 598 (3rd Cir., 1939), cert. den. 309 U.S. 671 (1940); see also <u>Federal United Corp.</u> v. <u>Havender</u>, 11 A. 2d 331 (Dela., 1940); <u>Langfelder</u> v. <u>Universal Laboratories, Inc.</u>, 6 F. Supp. 209 (Dela., 1946), aff'd. 163 F. 2d 804 (3rd Cir., 194 <u>Windhurst</u> v. <u>Central Leather Co.</u>, 149 A. 36 (N.J. Ch., 1930), af 153 A. 402 (N.J., 1931); <u>Adams</u> v. <u>U. S. Distributing Corp.</u>, 34 S 2d 244 (Va., 1945), cert. den. 327 U.S. 788 (1946); <u>Anderson</u> v. <u>Cleveland-Cliffs Iron Co.</u>, 87 N.E. 2d 384 (C. P. Cuyahoga County Ohio, 1948). See also <u>Otis & Co.</u> v. <u>S.E.C.</u>, 323 U.S. 624, 631, 638 (1945). As the cases show, the theory underlying this accep principle is that shareholders have notice of the merger provisi of applicable law, as was true here, and that because of such pr visions charter rights may be subject to adjustment.

3. <u>The factual basis in support of the Board's determination that the distribution terms of the Merger Agreement are fair.</u>

Whether the terms of the Merger Agreement attacked by appel are fair under the circumstances is, of course, a question of fa

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<u>35/</u> Although this issue was extensively briefed by the Board in motion for summary judgment, the District Court neither alluded the argument nor to the authorities cited in the Board's brief.

judgment. Clarke v. Gold Dust Corp., supra.

This fact question was never reached by the District Court, :e on its theory pro rata distribution was legally required ırdless of any facts or circumstances pertaining to the large :ease in savings accounts at Long Beach on and after April 2, ?.[36/]

Despite the exclusion of some evidence,[37/] upon which appellants .ed in support of their motion for summary judgment, appellants ıit that there is sufficient undisputed documentation to ıblish the fairness of the contested merger terms. First, it ›ertinent to note that Long Beach management was obligated to ·ain from any action which would be detrimental to the interests .ts shareholders. Borak v. J. I. Case & Co., 317 F. 2d 838, 842 \. 7, 1963), aff'd. 377 U.S. 426 (1964). Appellees have conceded ›ugh their proposed findings that Long Beach management played

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Under the District Court's theory, had the individuals con- :uting the management of Long Beach borrowed millions of dollars deposit in Long Beach in anticipation of either a liquidating .dend in the event there were an Article XV liquidation or a .ribution of stock in the event of a merger, or had management knowledge of the facts stood by and permitted other favored viduals to make such deposits, the depositors would have been .lly entitled to receive their pro rata share of Long Beach's worth despite the breach by management of its fiduciary re- .sibilities to its shareholders.

The records of this Court will disclose that appellants made ›tion to substitute corrected copies for certain lost depositions certain lost answers to interrogatories, that thereupon this 't remanded the matter to the District Court, that the District 't found that the depositions had not been filed or received in lence, that the answers to the interrogatories had been filed :not received in evidence, and that this Court then denied llants' motion.

an important role in the plan to bring large sums of money into Long Beach as follows (3R 1190, 1191, 1215):

> "28. In March-April, 1962, Long Beach Federal's officers and its Shareholders' Protective Committee wished to rehabilitate the precarious financial condition 38/ of the seized Association. They felt substantial new savings deposits were urgently and immediately required for such rehabilitation. The first few days of the restored Association upon its return to its founding management were believed to be the most critical time.
>
> "Louis H. Boyar had been a substantial customer of the Association for more than 20 years. He had assisted the Association with deposits in excess of $100,000 by he and his business associates in 1946-48, upon the Association's return from prior seizures. He was asked to again assist the Association in 1962.
>
> "In 1946-48 the run had been $10,000,000. In 1960 the run was seven times larger, amounting to about $69,000,000. Said Boyar was asked by said Association's representatives to obtain many millions of dollars of new deposits in as large amounts as possible. Boyar himself deposited in excess of $2,000,000. Members of Boyar's immediate family also made large deposits, some of more than $500,000 each.

38/ This is appellants' footnote, not a footnote copied from t[he] proposed findings. The Wilfand affidavit shows that Long Beach was not in a precarious financial position. As a result of the Settlement Agreement the Insurance Corporation had purchased at book value substantially all of Long Beach's non-earning loans, aggregating about $23 million. In addition, it had paid Long B[each] a $3 million premium in obtaining payment of the $45 million de[bt] owing to it by Long Beach. Its liquidity ratio was at the extr[a]ordinarily high level of 41% as compared to a regulatory requir[ement] of 7%. (3R 1374-1378). What it needed was not more savings, b[ut] more sound loans in which to invest its liquid resources and th[us] improve its earnings position.

"After said Association's savings deposits had grown from $30,000,000 on the day it was restored, April 2, 1962, to in excess of $60,000,000 before the end of May, 1962. Said Boyar and his family withdrew their personal deposits during June and July, 1962. They do not seek for themselves any share in the distribution of the net assets and surplus of said Association.

"29. Said Boyar contacted many persons of large resources, including those prominent in the entertainment and financial world, and suggested to them that they make substantial deposits in Long Beach Federal upon its return to its founding management. Among the persons so contacted were many who were already familiar with the possibility of a merger combining the Long Beach Federal into Equitable and who were stockholders, investment certificate owners, or others financially interested in Equitable Savings and Loan.

* * * *

"59. Many of the larger depositors are officers, attorneys shareholders or otherwise connected with Equitable Savings and Loan Association. Many of them borrowed the money with which to make their deposits and pledged their Long Beach Federal savings account as security for the amount so borrowed. By so doing they benefited both Long Beach Federal which received their deposits and Equitable which was able to merge with Long Beach Federal when Long Beach Federal became financially strong enough, through such new deposits, so the merger was financially feasible. . . ."

In short, appellees admit that the Long Beach management lberately had Mr. Boyar, a large Equitable stockholder, contact s wealthy friends to have them place large deposits in Long Beach. n of such individuals borrowed the funds which they thus invested. n were closely identified with Equitable as officers, attorneys tockholders. Some admittedly knew of the planned merger of n Beach and Equitable and others were presumably told of this

probability with the consequent gain to them. Indeed, common sense dictates that such large accounts would not have been opened at Long Beach (many with borrowed funds) except for the anticipated gain to result from the anticipated liquidation or merger.

Furthermore, the statistical data in the record (see <u>infra</u> pp. 8 - 11) gives a clear picture of the events which lead the Board to propose the adoption of the contested provisions. Wit out repeating all that has been heretofore reported, some of th basic figures bear summary. The following table is indicative of the nature of the deposits made on and after April 2, 1962:

Type of Account	No. of accounts as of April 22, 1960 when Long Beach deposits were about $96 million	No. of accounts opened or incre in period Apri to Nov. 1962 wh Beach dissoluti merger in conte
Over $100,000	1	77
$75,000 to $100,000	1	6
$50,000 to $75,000	0	34
$20,000 to $50,000	33	124

The record shows that accounts which increased by $10,000 more between April 2, 1962 and November 30, 1962 amounted to $ million; that $12.217 million of such amount were pledged to s loans; and that most of the holders of these accounts had no p connection with Long Beach (Exh. R). Similarly the data suppl by Long Beach to the California Commissioner (Exh. D referred par. XI of Exh. C, attached to Balderston affdvt. in support o

ıissioner's motion for summary judgment) shows that accounts :h increased by $20,000 or more between April 22, 1960 and still leposit on December 31, 1962, amounted to $17,826,712. Of this regate amount only $167,627 represented accounts in Long Beach ıpril 22, 1960 when its total savings amounted to approximately ımillion, clearly demonstrating that most of those affected by distribution terms of the Merger Agreement had no connection : Long Beach at the time when it was last in normal operation, had contributed nothing to its net worth.

As the record shows one family interest had on deposit as of :mber 31, 1962 $1,167,800, another man and his wife had 00,000 on deposit, another family interest had $917,000, two ıinent motion picture stars had respectively $300,000 and ,000 on deposit, attorneys for Equitable each had $250,000 on ısit etc. (Exh. D, referred to in Par. XI of Exh. C, attached 'alderston's affdvt. in support of the California Commissioner's :on for summary judgment, pp. 8-14, 18, Exh. S, Exh. C-29A). ı of these persons had ever had accounts in Long Beach prior pril 2, 1962.[39/]

' Exh. C-29A is a tabulation of accounts which increased by 000 or more between April 2, 1962 and November 30, 1962 ılied to the Board by Long Beach.
Exh. D referred to in Par. XI of Exh. C etc. is a list of ısits in Long Beach, showing an increase of over $20,000 on ous dates between April 22, 1960 and December 31, 1962, ished by Long Beach to the California Commissioner.
Exh. S is a list of deposits increased by $10,000 or more e April 2, 1962 and pledged as of November 30, 1962 -- and ing the amounts pledged.

In view of the size of these deposits, completely disproportionate to the normal Long Beach operations, it is reason to conclude that these deposits were made in the expectation of sharing in the division of the net worth upon liquidation or me

The action of the Board chairman (3R 1002) in insisting up the provisions herein contested was a bona fide effort to preve a raid upon the net worth by persons who had not contributed to growth. It should be remembered in this connection that these large and late depositors were entitled to and did receive the normal Long Beach dividends upon their total deposits, no matte when made nor whether pledged. And these dividends ranged from 4.5% to 4.8% (Exh. H).

Appellants submit in conclusion that if the question of fa ness is reached, the record supports a finding that the merger provisions relating to distribution of the Equitable guarantee stock were fair.[40/]

40/ If this Court should conclude that the documentation is in sufficient and that there is a genuine issue of fact as to the fairness of the distribution terms and as to the breach of fiduciary duty on the part of the Long Beach management, then t actions should be remanded to the District Court for trial. In this event, it is respectfully requested that the Court rule or the propriety of the limitations placed by the District Court c the appellants' right to inquire into the status, on and after September 10, 1963, of the pledged and other accounts adversel affected by the distribution terms of the Merger Agreement (Tr. 368-371, 377-380, 393-395; 3R 598-600, 698-709). The appellant wished to show that most, if not all, of those depositors had closed their accounts promptly or shortly after their rights t share in the Equitable stock distribution had become fixed on September 10, 1963.

4. <u>The Board's determination of fairness must prevail since there was a rational basis to support it.</u>

Under the Congressional delegation of power to the Board and r the applicable Board regulations, it was for the Board to rmine whether the Merger Agreement formula for distribution of table stock was fair and reasonable. The Board expressly found such distribution formula was "fair and equitable" (Exh. C-56). ress having lodged this regulatory power in the Board, the ts cannot substitute their views for those of the Board, if Board action has any rational basis. As the Supreme Court has l, "The judicial function is exhausted when there is found to be tional basis for the conclusions approved by the administrative ." <u>Mississippi Valley Barge Line Co.</u> v. <u>United States</u>, 292 282, 286-287 (1934). See also <u>S.E.C.</u> v. <u>Chenery Corp.</u>, 332 194 (1947); <u>American Power & Light Co.</u> v. <u>S.E.C.</u>, 329 U.S. 90 6); <u>Gray</u> v. <u>Powell</u>, 314 U.S. 402 (1941); <u>Rochester Telephone</u> <u>.</u> v. <u>United States</u>, 307 U.S. 125 (1939); <u>Cooper</u> v. <u>Woodin</u>, 72 d 179 (D.C. Cir., 1934); <u>Lucking</u> v. <u>Delano</u>, 122 F. 2d 21 (D.C. , 1941); <u>Hawkins</u> v. <u>Swan</u>, 52 F. 2d 688 (N.D. W. Va., 1931).

That the distribution formula insisted upon by the Board and rporated in the Merger Agreement as executed by Long Beach and table has a rational basis would seem, in light of the fore- g undisputed facts, to be self-evident. In substance the

formula, nullified by the District Court, took as its starting point each shareholder's November 30, 1962 account balance.[41] That balance was reduced by (1) then existing share loans or pledges, (2) subsequent withdrawals and (3) the amount by which the remaining balance exceeded the April 22, 1960 balance plus $10,000. The same formula was applied to "insiders", as define in Article VII of the Merger Agreement, provided that their participation was limited to an amount not in excess of their April 22, 1960 account balances. Generally speaking, under the Merger Agreement formula all Long Beach shareholders (except "insiders"), whether old or new, could participate in the distribution in an amount measured by account balances not in exce of $10,000, if their accounts were not pledged as of November 3 1962. Shareholders as of April 22, 1960, when Long Beach was taken over by the Board and Long Beach accounts amounted to $96 million, obtained additional participation rights measured by their April 22, 1960 balances, provided any part or all of such balances had remained in or had been reinvested in Long Beach a were not pledged as of November 30, 1962. The $10,000 figure w selected because that is the maximum amount of federal insuranc coverage.

This distribution formula represented an attempt by the Bo to restore a reasonable degree of equity to a situation badly w

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41/ After that date persons opening new accounts or adding to x ing accounts were required by Long Beach to waive their rights o participate in any distribution with respect to such new accou s or additions to old accounts.

he permitted, indeed solicited influx of accounts into Long h. Alternatively, of course, the Board might have concluded the situation was distorted beyond redemption and refused oval of the merger.

The reasonableness and rationality of the Board's approach udicially supported. The Ohio courts have recently had sion to consider similar problems in connection with the dis- tions of two mutual savings banks and the extent to which ous categories of the depositors in such banks could partici- in the distribution of net worth or stock. In In re Cleveland ngs Society, 25 Ohio Op. 2d 402, 192 N.E. 2d 518 (C.P. Cuyahoga ty, 1961), the court's resolution of the problem was expressed ollows (at pp. 529-530):

> ". . . this Court has taken into consideration . . . the fact that the Members, Trustees, Directors and Officers had knowledge of the transaction in December, 1957, and the fact that these men could be open to undue criticism. The Court, therefore, finds that the Members, Trustees and Officers of Society, and the Directors, stockholders and Officers of National, and their immediate families (wives and children living at home) shall not be permitted to participate in the remaining assets of Society to the extent of any increases in their accounts, other than by way of dividends, after December 1, 1957, nor shall they be permitted to participate in said remaining assets to the extent of any new accounts opened by any of such persons in Society after December 1, 1957.
>
> "The proposition of unjust enrichment was also raised as to third parties. This Court has examined the record, which includes every deposit of $25,000.00 or more made during the year 1958, and cannot find any pattern or any single instance

which would indicate prior knowledge, or an instance of unjust enrichment.

"Apart from the testimony and the evidence, this Court has also considered the fact that even though these proceedings have been going on for almost three years and have been given wide publicity, no one has come forth with any information or evidence which would indicate that any third person benefited by having had advance information of the transaction. There can be no doubt that the transaction was a well-kept secret.

"It is not likely that either the Superintendent of Banks or the Comptroller of the Currency would have approved or allowed the transaction to be completed if he had felt that the depositors of Society would have been harmed. Both had ample power to stop it. The record is clear that both were fully informed, actively participated to the extent required of them and in fact stated that in their opinion consummation of the Plan would benefit everyone including depositors." (Emphasis supplied)

The principles enunciated in Cleveland Savings Society wer later applied in In re Springfield Savings Society, Case No. 60 Court of Common Pleas of Clark County, Ohio (1965).42/ There the co fixed the participation rights of the mutual bank's depositors the amount of the lowest credit balance of each depositor, with certain exceptions, during the period commencing October 29, 19 and ending February 9, 1965. On the latter date the deposit liabilities of the mutual bank were assumed by the newly create

42/ A copy of the Court's opinion is reproduced in the Appendi 13a-52a. The Ohio Court of Appeals of Clark County, Ohio on Ju 1966, reversed and remanded the case to the Court of Common Ple but solely on the issue of the rights of the City of Springfiel participate in the distribution. This decision is reproduced i Appendix, pp. 1a-12a.

ingfield Bank", the surviving stock institution. October 29, was the date a general notice was sent to all depositors with ect to the combining of the institutions involved. The Court uded from participation in the distribution all deposits made r June 18, 1963 by persons with certain inside knowledge and rmation of the dissolution plan. June 18, 1963 was the date ussions first began relative to the change of the mutual savings itution into a stock company. The basis for the ban on dis-ltion with respect to those deposits was the receipt by the al bank of between fifty and sixty deposits from persons out-of Ohio who had no previous association with the institution. hat connection the Court observed that on June 18, 1963 a rities broker and financial analyst, who specialized in mutual ngs societies and who knew of the Cleveland Savings Society er, came to Springfield to discuss with the Society's management ossibility of terminating the Society's activities as a mutual itution. Thereafter this same broker helped to negotiate the al purchase and transfer of the Society's assets for which he compensated by the purchaser. The Court's discussion follows , pp. 37a-44a):

> ". . . between June 18, 1963 and December 5, 1963, and before the negotiations between buyer and seller for the purchase of petitioner's assets were formally undertaken, the same broker, without the knowledge or consent of petitioner, had notified by letter and otherwise a large number of persons, including his partners, his clients and prospective clients and their friends, of the likelihood of the conversion of petitioner

from a mutual savings bank, and recommended to these people that they make deposits of any of their 'idle funds' so that they might participate in the cash surplus should a sale be consummated, even though the current rate of interest would be lower than they could receive elsewhere. He also conveyed this information to a number of security brokers in Philadelphia and New York. . .

"The record further discloses that petitioner took notice of these unusual deposits and called the same to the attention of the broker, and at the instance and urging of petitioner, and beginning in November 1964, the broker contacted each of these depositors and made an effort to persuade them to withdraw their accounts, advising them that he had doubt as to the legality of their deposits, and advising them further that they would not be allowed in any event to participate in the distribution of the cash surplus. Most of these depositors followed his advice and withdrew their deposits, but fourteen of them failed and refused to do so.

"On May 19, 1965 a hearing was held for the specific purpose of considering the right of these depositors to participate in the plan. . . At that hearing the broker . . . (testified) . . . that these deposits were made in reliance on an anticipated windfall. He could offer no other explanation or reason as to why any of these persons or organizations from out of the state would make their deposits in a Springfield bank. . .

"Petitioner contends that by reason of these facts, . . . they should be excluded from participation in the distribution of its assets.

"It should be emphasized that the information upon which these depositors acted was not culled from financial statements or based on documents or announcements relating to the financial condition of petitioner and available to all potential investors alike. It came to them in the manner above described and there is no credible evidence in the record to the contrary.

"The Court is aware that, by the ordinary standards which apply to the 'market place', what happened

above may be considered normal and proper, and the Court sees no need to make further comment on the ethical considerations that may be involved. However, it must be remembered that we are not dealing here with the practices of the 'market place'. Banks are in a different and special category. They provide the life blood for our economy. The stability of the whole community may be undermined by any suspicion of manipulation or speculation in any of its affairs. . .

"It should be noted that the trustees of the Springfield Savings Society, undoubtedly mindful of the sensitive nature of their position and anxious to avoid any suspicion of unjust enrichment accruing to themselves by reason of their access to confidential information, voluntarily renounced for themselves, their wives, and any of their children who lived with them after June 18, 1963, the right to participate in the surplus fund.

"These fourteen depositors differ from the trustees only in that they themselves were not officers of petitioner or related to them, but they are otherwise alike in that they became privy to the same confidential information accessible to the others on June 18, 1963, and thereafter, and before the same became a matter of public knowledge.

"Incidentally, the Cleveland case recognized the validity and logic of this reasoning and disqualified from participation those persons who became depositors after the negotiations for the sale of the Cleveland Savings Society began or increased their deposits after that date, on the ground that, having had information as of that date, they were barred. As previously noted, the record in the Cleveland case discloses that only members and trustees of the two banks in Cleveland fell in that category, and thus there was no need in that case to consider the effect of this knowledge on any other persons.

"This Court is of the opinion that the same reasons which led to the disqualification of the trustees and members of the Cleveland banks, and which by the voluntary action of the trustees of petitioner bars them and their families from participating, applies with equal weight to the fourteen depositors under consideration.

* * * * *

"The relationship between a mutual savings bank and its depositors is not merely one of debtor and creditor, but one of agent and principal as well. The relationship was defined as long ago as 1896 by the then Circuit Court for this very district in a case, oddly enough, involving the same petitioner but concerned with issues unrelated to those in the instant case. The Court refers to Collett, Treas. v. Springfield Savings Society, 13 O.C.C.R. 131. The Court in that case discussed the reasons for the existence of mutual savings societies and concluded that, while the relation of bank and general depositor is simply the ordinary one of debtor and creditor, 'the relation of savings society, such as defendant, and depositor is that of agent and principal.' It is elementary that an agent is regarded as a fiduciary, and the relationship between agent and principal is one that implies trust and confidence and unqualified exercise of loyalty, fidelity and good faith in the execution of its responsibilities. (See 2 O.J. (2d) 168, etc.)

* * * * *

"The Court wishes also to state that no criticism or slur is intended for any of the fourteen depositors, who, as far as the record discloses, acted in good faith and seized an opportunity to make what was represented to them to be a highly lucrative investment. They are not being penalized by any decision reached by this Court. Their accounts are secure, and they, together with all other depositors, are entitled to receive and keep the interest accumulated to their accounts.

"However, the Court does find that each of the fourteen depositors did have knowledge or information that the officers or trustees of the petitioner had discussed with individuals not associated with the Society the possibility of terminating its activities as a mutual savings bank and knew that the officers of an investing corporation had expressed an interest in exploring the acquisition of the Society, and that their deposits were made as a result of such information and for the sole purpose of speculating upon the possibility of participating in this surplus and were not made within the usual and normal course of business."

The facts present here are quite analogous to and indeed nger than those in the Springfield Savings Society case. Here, ontrast to Springfield, the Long Beach management actively icipated in the solicitation of savings accounts at Long Beach, unts opened for the purpose of obtaining a windfall. The ciples applied by the Board in insisting upon the distribution s of the Merger Agreement are consonant with those applied by Ohio courts and with the Board's statutory and regulatory responsibilities. Clearly on the basis of the Ohio precedents alone, Board action in insisting upon the restrictive distribution s should have been upheld as fair and equitable.

IV. THE CALIFORNIA COMMISSIONER IS AN INDISPENSABLE PARTY TO THE ACTIONS; SINCE HE WAS NOT SUBJECT TO SUIT IN THE DISTRICT COURT, THE ACTIONS MUST BE DIMISSED.

The District Court concluded that the appellant California issioner was subject to its jurisdiction and accordingly found nnecessary to pass on the question of whether he was an indisable party to the actions, since he was at least a proper party F. Supp. at p. 590).43/

The California Commissioner under state law, supra, pp. 21-22, required to approve the Merger Agreement in order for it to be effective and he was also required to approve the issuance of

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The California Commissioner was not and was never made a party ivil Action No. 63-1072 PH, the action commenced in the District t on September 10, 1963.

the Equitable guarantee stock which is the subject matter of th litigation. The Commissioner did approve the Merger Agreement D-7), including the disputed Article VII, and did authorize the issuance of Equitable stock conditioned on the stock being distributed in accordance with the terms of Article VII (Exh. D-8) A challenge to the merger agreement is a challenge to the admin trative action of the California Commissioner and in these circ stances he is an indispensable party. MacArthur Liquors, Inc. Palisades Citizens Association, Inc., 265 F. 2d 372 (D.C. Cir., 1959); Blackmar v. Guerre, 342 U.S. 512 (1952); Hicks v. Summer 261 F. 2d 752 (D.C. Cir., 1958), cert. den. 359 U.S. 959 (1959) the cases there cited. As was stated in the MacArthur Liquors supra, at p. 374:

> "The members of the Board are indispensable parties to a suit which seeks to set aside the Board's action."

The test for an indispensable party was set forth by this in State of Washington v. United States, 87 F. 2d 421, 427-428 as follows:

> "(1) Is the interest of the absent party distinct and severable? (2) In the absence of such party, can the court render justice between the parties before it? (3) Will the decree made, in the absence of such party, have no injurious effect on the interest of such absent party? (4) Will the final determination, in the absence of such party, be consistent with equity and good conscience?"

This test has been cited with approval in Moore's Federal Pract Vol. 3, p. 2155, and again recently by this Court in McShan v.

rill, 283 F. 2d 462 (1960). See also Shields v. Barrow, 17 rd (58 U.S.) 130 (1854). Applying this test, it is obvious the interest of the Savings and Loan Commissioner is not rable from that of the other parties to the lawsuit nor can a ee be entered without affecting his interest. Thus, under the set forth by this Court, the California Commissioner clearly n indispensable party.

Since, as the California Commissioner has demonstrated,[44/] the rict Court had no jurisdiction over him, and since, as we have n, he was an indispensable party in this litigation, the three ons should have been dismissed.

CONCLUSION

The judgments of the District Court should be reversed and the ons remanded to the District Court for the entry of orders dis-ing the actions with prejudice on the following grounds:[45/]

So as not to burden the Court with unnecessary repetition, the llants Board and Insurance Corporation adopt the arguments set h in the brief of the California Commissioner on the issue of District Court's jurisdiction over him.

If this Court should agree with the legal theories of the Distric t in all respects, it is respectfully requested that the judgments he District Court be modified with respect to the 71,183 shares of table stock which it ordered reserved for use in the payment of s and attorney fees, if any, when allowed (3R 1648). While the rict Court's judgments did not clearly set forth the source from h the 71,183 shares were derived, the appellees' proposed judgment lies this information (3R 1528-1533). Of the 71,183 shares, 59,10 esent the number of shares attributable to former Long Beach share ers who would have been eligible to receive the shares had they tained their accounts in Long Beach until September 10, 1963. In tion, 6,154 shares represent the number which would have been dis-utable with respect to the share accounts opened at Long Beach

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1. The District Court had no power to change the distributi terms of the Merger Agreement and to order distribution of the Equitable stock on a pro rata basis and, in the circumstances, th aggrieved Long Beach shareholders, not having sought to enjoin th merger, are not entitled to any relief.

45/ (Continuation)
after April 2, 1962 in the amount of $560,000 in connection with transaction involving the payment of past due attorney fees to counsel for Long Beach and with respect to which accounts the attorney's alleged participation rights were waived. The remaini 5,923 shares resulted from alleged errors in computing the amount distributable under the consent order of October 29, 1963. Appe lees characterized the 71,183 shares as abandoned (3R 1529). Apparently the District Court agreed because of the terms of its judgments. As noted therein (3R 1706), 58,179 of such shares rep sented part of the 585,821 shares of stock which should have beer distributed under the consent order of October 29, 1963 to Long B shareholders who had nothing to gain from the litigation and conc ing which there was no dispute. The remaining 13,004 shares of t 71,183 reserved for costs and counsel fees constitute part of the 205,829 shares which are in dispute and which are distributable under the District Court's judgments to shareholders who are sub to the restrictive provisions of the Merger Agreement.

The District Court order allowing attorney fees demonstrates disposition made of the 71,183 shares (App., p. 80a). The court mitted them to be used in the payment of attorney fees to counse Long Beach and the Shareholders' Protective Committee. No other shares were reserved for that purpose. As a result, those Long B shareholders who had nothing to gain from the litigation institut and prosecuted by the Shareholders' Protective Committee and by L Beach and to whom 58,179 of the 585,821 undisputed shares should been distributed under the consent order of October 29, 1963, are quired to pay for a portion of the allowed attorney fees. Those shareholders were represented by the Board and not by the Shareh Protective Committee (footnote 2, p. 4). The shareholders who stand to benefit from the District Court's judgments and who were represented by the Shareholders' Protective Committee are requir to utilize only 13,004 shares of the 205,829 disputed shares, wh are distributable to them under such judgments, towards payment attorney fees. The inequity and unreasonableness of this result self-evident.

The District Court judgments should be modified so that tho former Long Beach shareholders who gained nothing from this liti gation, but whose participations rights were lessened by 205,829

(Continued on page 69)

2. In any event, neither the law, the Long Beach Charter, the Settlement Agreement required a pro rata distribution and, light of the undisputed material facts, the distribution terms e fair and equitable and therefore valid.

3. The California Commissioner was an indispensable party to actions and, since he was not subject to suit in the District rt, the actions must be dismissed.

In the event the Court should conclude that a pro rata distribution of Equitable stock was legally required, regardless of facts and circumstances present here, and that laches does not relief in the circumstances, the cases should be remanded to District Court with instructions to set aside the merger, and take appropriate action, in light of all now existing facts and cumstances, to divest Equitable of Long Beach assets and

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(Continuation)
res of Equitable stock, should not bear any part of the legal s which may be finally awarded in these actions; the 58,179 res, which were reserved by the District Court for payment of orney fees and which constitute part of the 585,825 shares distributable to such Long Beach shareholders under the October 29, 3 consent order, should be ordered distributed to them. If any itable stock is to be reserved for the payment of legal fees, it uld be out of the 205,829 shares of stock distributable to those g Beach shareholders, represented by the Shareholders' Protective mittee, who were subject to the restrictive provisions of the ger Agreement, and who benefit by the District Court's judgments. only fund created or preserved through this class action litiion is the disputed 205,829 shares. It is only this fund which uld be employed for payment of counsel fees. Abbott, Puller & rs v. Peyser, 124 F. 2d 524 (D.C. Cir., 1941); United States v. key, 98 F. Supp. 431 (D. Montana, 1951).

liabilities so that a new merger agreement, without the illegal provisions, may, if Long Beach and Equitable should so desire, b entered into and submitted for the necessary approvals or disapprovals by the respective members and stockholders of Long Bea and Equitable and by the federal and state supervisory authorit

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CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Cou of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

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